

**DEVELOPMENT FUND FOR IRAQ:  
POLICY GUIDANCE NEEDED TO  
ENHANCE ACCOUNTABILITY OF  
USACE-MANAGED FUNDS**

**SIGIR 10-006  
OCTOBER 29, 2009**

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# SIGIR

Special Inspector General for IRAQ Reconstruction

## Summary of Report: SIGIR 10-006

### Why SIGIR Did this Audit

The Development Fund for Iraq (DFI) was created by United Nations Security Council Resolution 1483 for: (1) economic reconstruction of Iraq, (2) continued disarmament of Iraq, (3) costs of Iraqi civilian administration, and (4) other purposes benefiting the Iraqi people. The funds were to be used in a transparent manner. During the Coalition Provisional Authority's (CPA) administration of Iraq, the CPA Administrator managed DFI funds, and CPA Regulation 2, "Development Fund for Iraq" describes the responsibilities for the administration, use, accounting, and auditing of the DFI. When the CPA was disestablished in June 2004, responsibility for administering DFI funds eventually shifted to the Joint Contracting Command-Iraq/Afghanistan. The U.S. government's stewardship of the DFI ended on December 31, 2007, and all remaining funds were to be returned to the Government of Iraq (GOI), per a GOI request.

Several Department of Defense (DoD) components received DFI funds, including the U.S. Army Corps of Engineers (USACE). The purpose of this audit is to determine whether USACE properly accounted for DFI funds it received.

### Recommendations

The Special Inspector General for Iraq Reconstruction (SIGIR) recommends the Under Secretary of Defense (Comptroller)/Chief Financial Officer provide guidance to USACE on the 1) use and ultimate disposition of DFI funds that it and one of its contractors are currently holding, 2) whether GOI funds should have been used to pay reimbursable work order expenses, and 3) how interest that might have been earned by several contractors on disallowed payments should be used.

### Management Comments

We received comments from the Office of the Undersecretary of Defense (Comptroller) and USACE on a draft of this report. The comptroller concurred with the report recommendations. USACE provided detailed comments that we included as appropriate.

October 29, 2009

## DEVELOPMENT FUND FOR IRAQ: POLICY GUIDANCE NEEDED TO ENHANCE ACCOUNTABILITY OF USACE-MANAGED FUNDS

### What SIGIR Found

SIGIR has identified a number of policy issues related to the management of DFI funds that require DoD attention. To date, SIGIR has identified \$27.5 million in DFI funds for return or potential return to the GOI—\$13.1 million was returned in March 2009 based on earlier SIGIR work; in this report, we identify \$14.4 million that may potentially be available for return.

After some delays, USACE provided a listing of DFI-funded contracts totaling \$2.4 billion and is working on providing a listing of its expenditures. However, we did not confirm this data at the time our audit work was completed. USACE assumed responsibility for many DFI activities initiated by earlier reconstruction organizations, and a transaction-based accounting system was not used early in the U.S.-reconstruction program. Instead, data was recorded on spreadsheets, and cash was disbursed but not entered into USACE's database. In addition, separate accounting codes were not established to segment DFI from other funding sources.

Although the GOI requested that all DFI funds be returned to it by December 31, 2007, USACE is currently holding about \$3.0 million of DFI funds pending final close-out of some DFI contracts. This situation occurred because USACE entered into contracts making the U.S. government responsible for all costs through the close-out of the contract. SIGIR understands that USACE may require funds associated with the DFI contracts. However, DoD policy guidance is lacking on whether it is appropriate to hold or use DFI funds to meet these obligations.

SIGIR notes a USACE contractor is holding \$2.2 million in DFI funds. Specifically, in November 2006, USACE issued contract modifications that led to three contractors—Perini Management Services, Washington Group International and Fluor Intercontinental—receiving about \$11.2 million for costs that had not been incurred prior to the time they submitted vouchers. The Defense Contract Audit Agency (DCAA) subsequently disallowed the payments, and two of the contractors, Perini and Fluor, returned their funds. These funds were later returned to the GOI. However, Washington Group returned only about \$3.0 million of the \$5.2 million it received and continues to hold about \$2.2 million for work it said was completed but not yet approved for payment. DCAA is currently auditing the data supporting the \$2.2 million. DoD may also have an opportunity to collect interest earned on funds provided by USACE to several contractors but disallowed by DCAA.

USACE stated it has used \$9.2 million of GOI funds to cover unpaid expenses from earlier reimbursable work orders that it believes were the responsibility of the GOI; \$8.9 million for actual contract costs, and \$0.3 million for labor and overhead. This payment may be inconsistent with guidance from the Under Secretary of Defense (Comptroller)/Chief Financial Officer stating that residual advanced seized funds should not be used for this purpose. During our review we have been unable to separately account for DFI funds and seized asset funds because the funds have been commingled. We also have not been able to verify whether GOI funds should have been used to pay these expenses.



## SPECIAL INSPECTOR GENERAL FOR IRAQ RECONSTRUCTION

October 29, 2009

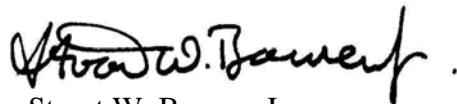
MEMORANDUM FOR U.S. UNDER SECRETARY OF DEFENSE  
(COMPTROLLER)/CHIEF FINANCIAL OFFICER  
COMMANDING GENERAL, U.S. ARMY CORPS OF ENGINEERS

SUBJECT: Development Fund for Iraq: Policy Guidance Needed To Enhance Accountability of USACE-managed Funds (SIGIR 10-006)

This report is provided for your review and use. It focuses on the U.S. Army Corps of Engineers' accountability for funds received from the Development Fund for Iraq. We performed this audit in accordance with our statutory responsibilities contained in Public Law 108-106, as amended, which also incorporates the duties and responsibilities of inspectors general under the Inspector General Act of 1978. This law provides for independent and objective audits of programs and operations funded with amounts appropriated or otherwise made available for the reconstruction of Iraq, and for recommendations on related policies designed to promote economy, efficiency and effectiveness and to prevent and detect waste, fraud, and abuse. This audit was conducted as Project 9011. We plan to conduct a series of audits to determine whether the Department of Defense and its components, as well as other U.S. agencies, have properly accounted for DFI funds they have received.

We considered comments from the Office of the Under Secretary of Defense (Comptroller) and USACE when preparing this report. The comments are addressed in the report where applicable, and the letter is included in Appendix D of this report.

We appreciate the courtesies extended to our staff. For additional information on the report, please contact David Warren, Assistant Inspector General for Audits, (703) 604-0982/ [david.warren@sigir.mil](mailto:david.warren@sigir.mil), or Glenn Furbish, Principal Deputy Assistant Inspector General for Audits, (703) 604-1388/ [glenn.furbish@sigir.mil](mailto:glenn.furbish@sigir.mil).



Stuart W. Bowen, Jr.  
Special Inspector General for Iraq Reconstruction

cc: U.S. Secretary of State  
U.S. Ambassador to Iraq  
U.S. Secretary of Defense  
Assistant Secretary of the Army (Financial Management and Comptroller)  
Commander, U.S. Central Command  
Commanding General, Multi-National Force-Iraq  
Commanding General, Joint Contracting Command-Iraq/Afghanistan

**Draft Report  
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# **Table of Contents**

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<b>Introduction</b>	<b>1</b>
Background	1
Objective	3
<b>Policy Guidance Is Needed To Enhance Accountability of USACE-managed Funds</b>	<b>4</b>
USACE’s DFI Funding Remains Under Review	4
One USACE Contractor Is Still in Possession of DFI Funds	5
The Majority of DFI Funds Returned but Some Remain In a Suspense Account	6
Use of GOI Funds May Be Inconsistent With DoD Guidance	7
Other DoD Components May Have Retained DFI Funds	8
<b>Conclusions, Recommendations and Lessons Learned</b>	<b>9</b>
Conclusions	9
Recommendations	9
Lessons Learned	9
<b>Management Comments and Audit Response</b>	<b>10</b>
<b>Appendix A—Scope and Methodology</b>	<b>11</b>
<b>Appendix B—Acronyms</b>	<b>15</b>
<b>Appendix C—Audit Team Members</b>	<b>16</b>
<b>Appendix D—Management Comments</b>	<b>17</b>
<b>Appendix E—SIGIR Mission and Contact Information</b>	<b>20</b>



## Development Fund for Iraq: Policy Guidance Needed To Enhance Accountability of USACE-managed Funds

SIGIR 10-006

October 29, 2009

### Introduction

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U.S. government agencies received more than \$2.4 billion from the Development Fund for Iraq (DFI) to administer and oversee reconstruction contracts for the betterment of the Iraqi people, according to independent audit reports of the Fund prepared for the Government of Iraq (GOI) and the International Advisory and Monitoring Board.<sup>1</sup> The DFI was established by the Administrator of the Coalition Provisional Authority (CPA), and recognized by a resolution of the United Nations Security Council,<sup>2</sup> to be used in a transparent manner to provide for: (1) humanitarian needs of the Iraqi people, (2) economic reconstruction and repair of Iraq's infrastructure, (3) continued disarmament of Iraq, (4) cost of Iraqi civilian administration, and (5) other purposes benefiting the people of Iraq. The Department of Defense (DoD) was one of several U.S. agencies to participate in the DFI program, and the U.S. Army Corps of Engineers (USACE) was one of several DoD components to receive DFI funds. The total amount of DFI funds that USACE received is unclear as referenced in the body of the report.

GOI authorization for U.S. administration of DFI funds ended on December 31, 2007. The Special Inspector General for Iraq Reconstruction (SIGIR) initiated an audit (Project 9011) of USACE's use of DFI funds in response to a hotline tip regarding possible irregularities with USACE's contracting activities. SIGIR is providing this report on DFI funds held by USACE and plans to issue a series of reports to determine whether other U.S. government agencies are holding DFI funds.

### Background

The DFI was established in May 2003 pursuant to the power vested in the Administrator of the CPA.<sup>3</sup> During the CPA's administration of Iraq, the CPA Administrator managed DFI funds, and CPA Regulation 2, "Development Fund for Iraq" described the responsibilities for the administration, use, accounting, and auditing of the DFI. The DFI was funded from export sales of petroleum, petroleum products, and natural gas from Iraq. In addition, surplus funds from the United Nations Oil-for-Food Program as well as frozen assets were transferred to the fund. The Federal Reserve Bank of New York holds DFI funds in two accounts: the Central Bank of Iraq account—known as the main account—and an account available to U.S. government agencies for use in administering DFI contracts—known as the secondary or sub-account. On June 28, 2004, the beginning balance in the DFI sub-account was \$800 million. The United Nations also set up the International Advisory and Monitoring Board to monitor and audit the use of the DFI.

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<sup>1</sup> See Appendix A for a list of these reports.

<sup>2</sup> United Nations Security Council Resolution 1483, dated May 22, 2003.

<sup>3</sup> The CPA was established in April 2003 for the temporary governance of Iraq following the invasion of Iraq.

Upon dissolution of the CPA in June 2004 and the transfer of sovereignty to the Interim GOI, DFI's administrative responsibilities were transferred to the Iraq Ministry of Finance. From June through December 2004, the Iraq Minister of Finance assigned responsibility to the U.S. government Program Management Office<sup>4</sup> in Iraq to monitor and confirm performance, certify and/or make payments, and otherwise administer certain DFI funded contracts and grants.

The Minister of Finance extended this authority on several occasions and to different U.S. organizations—the Joint Contracting Command-Iraq/Afghanistan (JCC-I/A) is the last organization to have such authority. The Minister of Finance, in a letter to the Commander, JCC-I/A, agreed to extend JCC-I/A's authority to administer and complete payment of remaining money due on DFI-funded contracts until December 31, 2007. The Minister of Finance specified that JCC-I/A should not award any new contracts after December 31, 2007, nor renew or extend any previously awarded contracts. The Minister also noted that all contracts were to be completed by December 31, 2007 and remaining funds were to be transferred from the secondary account to the main account within the Federal Reserve Bank of New York.

Upon notification of program termination, JCC-I/A took immediate steps to close out its DFI activities. For example, in November 2007, JCC-I/A began sending letters notifying contractors that the contract administration authority granted to it by the GOI would cease on December 31, 2007. JCC-I/A also directed that all remaining cash being held for DFI activities be returned to the GOI.<sup>5</sup> In contrast, as of September 2009, U.S. Army Corps of Engineers (USACE) continued to hold contracts open and retain DFI funds. USACE officials stated that DFI funds might be needed to pay cost reimbursable expenses on contracts it entered into, on behalf of the U.S. government, for DFI activities.

USACE is headquartered in Washington, D.C. and within its headquarters, the Directorate of Military Programs is responsible for coordinating efforts in Iraq and Afghanistan. USACE's Transatlantic Programs Center (TAC) in Winchester, Virginia, is a subordinate element of USACE that reports to USACE-Headquarters, and provides administrative support on behalf of contracting officials working within the theater of operations. The USACE Gulf Region Division was established as a provisional Major Subordinate Command after operations in Iraq exceeded TAC's capabilities.<sup>6</sup> The USACE Finance Center in Millington, Tennessee is responsible for posting disbursements and maintaining supporting documentation through an automated information system known as the Corps of Engineers Financial Management System (CEFMS).

SIGIR's Investigations Directorate, based on a hotline tip, conducted a preliminary investigation that centered on a contractor that had submitted a voucher for a large dollar amount for costs that had not been incurred. The Investigations Directorate determined the voucher was submitted at the direction of USACE but it concluded there was no criminal wrongdoing involved. In response to SIGIR's investigation, in March 2009, USACE returned to the GOI about \$13.1 million in DFI funds it was holding.

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<sup>4</sup> The Program Management Office was originally established to direct, coordinate and oversee the contracting organizations for the Iraq Relief and Reconstruction Fund.

<sup>5</sup> *Attestation to Development Fund for Iraq Cash in the Possession of the Joint Area Support Group-Central*, SIGIR 08-012, 3/13/2008.

<sup>6</sup> USACE has announced the inactivation of the Gulf Region Division effective October 23, 2009.

## **Objective**

SIGIR plans to conduct a series of audits to determine whether DoD and its components, as well as other U.S. agencies, have properly accounted for DFI funds they received. This report on USACE represents the first in this series of reports. Our reporting objective is to determine USACE's accountability for funds it received from the DFI. For a discussion of the audit scope and methodology, see Appendix A. For a list of the acronyms used in this report, see Appendix B. For a list of the audit team members, see Appendix C. For management comments, see Appendix D. For the SIGIR mission and contact information, see Appendix E.

# **Policy Guidance Is Needed To Enhance Accountability of USACE-managed Funds**

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SIGIR's review of USACE's DFI fund management identified a number of issues that raise questions about how DFI funds can and should be managed and used. For example:

- To date, USACE has not provided us with a complete listing of its DFI fund activities. Numerous organizational changes in the management and accounting of DFI funds prior to USACE assuming responsibility contributes to this problem. At the conclusion of our audit, USACE officials provided a list of funds it received but information on fund use is still being gathered.
- Although the GOI apparently directed that payment of remaining money due on DFI-funded contracts was to be completed by December 31, 2007, USACE currently has about \$3.0 million in DFI funds for potential liabilities associated with open reconstruction contracts, and one USACE contractor has about \$2.2 million it said was for work that had been completed but not yet approved for payment. The Defense Contract Audit Agency (DCAA) is currently auditing the data supporting the \$2.2 million.
- USACE used \$9.2 million of GOI funds to pay for reimbursable work order expenses, which may be inconsistent with guidance provided by the Office of the Secretary of Defense.

SIGIR also notes that DoD lacks clear policy guidance on the handling and continued use of DFI funds, such as those held by USACE.

## **USACE's DFI Funding Remains Under Review**

After some delays, USACE provided a listing of DFI-funding it received totaling \$2.4 billion. Initially, SIGIR asked USACE to identify all of its DFI-funded activities from the start of the DFI in the spring of 2003 until the end of the U.S. government's control of DFI in December of 2007. SIGIR was initially provided reports that did not include all USACE DFI activities. For example, SIGIR was provided two different accounts: the first list identified 24 projects with a combined value of about \$127.8 million; and the second list identified 41 projects with a combined value of about \$143.4 million. We discussed these concerns with USACE officials who provided a more comprehensive list showing the amount of DFI funds USACE received was about \$2.4 billion. However, we did not confirm this data nor did we receive information on fund use by the time our field work was completed. USACE officials said that a contributing factor for the delayed response was the lack of a single DFI accounting code in the Defense Finance and Accounting Service regulations.

USACE's difficulty in identifying the universe of DFI-funded activities stems from long standing weaknesses in DFI accounting processes, some occurring before USACE assumed responsibility for DFI projects initiated by other organizations. For example, independent audit reports completed for the GOI and the International Advisory and Monitoring Board in 2005

indicated that U.S. government agencies did not maintain a complete and accurate database of contractual commitments signed by the former CPA. In addition, independent auditors reported that USACE did not routinely monitor the amount of cash received from the DFI against project disbursements and remaining obligations on DFI-funded contracts and task orders. As of the most recent audit report,<sup>7</sup> dated December 31, 2008, the auditors had no indication that the deficiencies had been corrected.

USACE officials stated that they assumed responsibility for many DFI activities initiated by earlier reconstruction organizations, and a transaction-based accounting system was not used early in the U.S.-reconstruction program. Instead, data was recorded on spreadsheets, and cash was disbursed but not entered into USACE's database. In addition, separate codes were not established to segment DFI from other funding sources.

## One USACE Contractor Is Still in Possession of DFI Funds

One USACE contractor is still in possession of \$2.2 million in DFI funds. In November 2006, USACE-TAC issued modifications to DFI contracts involving Perini Management Services, Incorporated; Washington Group International, Incorporated; and Fluor Intercontinental, Incorporated, which required the three contractors to bill the U.S. government a total of about \$11.2 million for costs they did not incur prior to the time they submitted vouchers. In submitting their vouchers, the contractors were instructed to send them directly to USACE-TAC. USACE officials told us that they ordered the modifications because they understood that unused DFI funds were going to be turned back to the GOI on December 31, 2006.<sup>8</sup> The officials stated that if they did not retain the funds, they may not have the money to pay outstanding vouchers on DFI contracts. Several USACE officials were aware of the contract modifications and assisted in developing the language for them, including that for submitting the invoices directly to TAC rather than through DCAA, which is the normal process. However, the modifications specified that the payments would be subject to future DCAA audits. In 2008, DCAA issued audit reports on all three contractors and disallowed the payments made by USACE.

Washington Group's contract modification totaled approximately \$1.5 million, and Washington Group was instructed to submit a final invoice directly to the contracting officer at TAC in the amount of all remaining funding under the contract. Washington Group's invoice totaled about \$5.2 million. DCAA issued an audit report<sup>9</sup> on Washington Group, dated September 5, 2008, which stated, "Although we reconciled the voucher amounts to its books of record, we determined that \$5,203,045 of the billed costs were not actually incurred." When USACE sent a letter requesting the funds be returned, Washington Group requested an extension in order to provide documentation for costs it incurred and for which it believes it should be compensated. As a result, Washington Group did not return about \$2.2 million of the approximately \$5.2 million that it had received from USACE. DCAA is currently auditing Washington Group's vouchers to determine what portion of the costs can be validated and retained.

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<sup>7</sup> *Development Fund for Iraq Management Letter Arising from Audit, Independent Auditors Report, KPMG, 12/31/2008.*

<sup>8</sup> The GOI extended U.S. administration of the DFI through December 31, 2007.

<sup>9</sup> *Report on Voucher No. 1409-27, November 9, 2006 Under Prime Contract No. DACA 78-03-D-0004, Task Order 0002, DCAA Audit Report No. 4261-2008W1790004, 9/5/2008.*

Perini and Fluor also received contract modifications for costs that had not been incurred prior to the time they submitted vouchers. The modifications for Perini and Fluor totaled approximately \$1.7 million and \$3.5 million, respectively. Perini billed USACE, as directed, for all funds remaining on the contract, which totaled \$2.5 million. DCAA issued audit reports<sup>10</sup> for both Perini, dated January 31, 2008, and Fluor, dated August 20, 2008, disallowing the payments made by USACE. Both Perini and Fluor returned the full amount of the disallowed payments when USACE sent letters requesting the funds be returned.

Perini returned two checks to USACE—one for the principal amount of approximately \$2.5 million and one for \$300,290 in interest earned on the funds sent by USACE and disallowed by DCAA. USACE was not aware that interest had been earned on the funds that it provided under the contract modifications until Perini brought it to their attention. USACE responded to Perini with a letter stating, “...because funds obligated to contracts are for specific authorized amounts, the United States Government is not able to process the interest amount generated by GOI funds belonging to the GOI that were obligated to this contract...” Accordingly, USACE directed Perini to transfer the interest earned to the GOI and provided procedures on how to do it. While evidence shows that Perini returned the \$300,290 to the GOI, USACE did not contact Washington Group or Fluor to determine whether they also had earned interest on the USACE-provided funds. According to USACE officials, under the Federal Acquisition Regulation, the government does not charge a contractor interest until it identifies a debt and issues a demand letter for that debt. Moreover, contract debts do not begin to accrue interest until they remain unpaid for 30 days after the date of the demand payment. While this is true, SIGIR questions why contractors are permitted to retain interest earned on money that was subsequently returned to the GOI.

In an email a USACE Headquarters official stated that it would direct the Middle East District to contact Washington Group and Fluor to seek recovery of any interest earned on DFI funds held by those contractors that were subsequently disallowed.

## **The Majority of DFI Funds Returned but Some Remain In a Suspense Account**

USACE officials returned the majority of USACE’s DFI funds to the GOI in early 2009 but continue to hold additional funds that may also need to be returned. USACE officials provided documentation showing that on March 3, 2009, it transferred approximately \$13.1 million to the GOI. Our analysis of this transfer shows that about \$5.9 million originated from DFI funds returned by Perini and Fluor when DCAA disallowed payment of those funds and \$7.2 million came from suspense accounts maintained by USACE. USACE officials stated that, in response to SIGIR’s investigation, they returned these funds to the GOI.

According to USACE officials, as of September 2009, its Finance Center still held approximately \$3.0 million of DFI funds in a suspense account. The majority of these funds, or

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<sup>10</sup> Report on Voucher No. 151-FM-061, November 9, 2006 Under Prime Contract No. DACA 78-03-D-006 D.O.0002, DCAA Audit Report Mo. 02161-2008V17900002, 1/31/2008. Report on Voucher No. 58, November 9, 2006 Contract No. DACA 78-03-D-0005, Task Order 0006, DACA Audit Report No. 4411-2008N17900005, 8/20/2008.

about \$2.9 million, represent funds returned to USACE by Washington Group. USACE officials stated they were holding approximately \$3.0 million to pay possible claims against the U.S. government for cost-reimbursable expenses on DFI-funded contracts that have not been financially closed. USACE officials stated they used DFI funds to award cost-reimbursable contracts between themselves and a variety of U.S. and Iraq-based providers. The officials noted that under cost-reimbursable contracts, the U.S. government remains liable until expenditures, including applicable overhead rates, are finalized. In contrast, USACE officials told us that JCC-I/A awarded contracts under the DFI program on behalf of the GOI; therefore, the U.S. government was not liable. However, USACE-TAC officials stated that if this was the preferred method of contracting, no one ever communicated it to them.

## **Use of GOI Funds May Be Inconsistent With DoD Guidance**

USACE stated that it used about \$9.2 million in GOI funds to reimburse itself for expenses incurred on earlier reimbursable work orders. However, this action may be inconsistent with DoD guidance on the use of DFI. USACE had requested guidance from the Under Secretary of Defense (Comptroller)/Chief Financial Officer concerning the propriety of using DFI funds to cover unpaid expenses that they believed were the GOI's responsibility. USACE's request for guidance notes that it had accumulated an estimated \$32.5 million in expenses to support contracts awarded with DFI funds. The memorandum states that, of this amount, USACE had previously received about \$23.3 million from the GOI, leaving an unpaid balance of approximately \$9.2 million. The memorandum also indicates that USACE had exhausted all available means in-country to obtain reimbursement for the unpaid balance.

On February 25, 2008, a USACE official sent a message to the Under Secretary of Defense (Comptroller) Accounting and Finance Policy officer asking if DoD legal counsel had consulted with international lawyers concerning the possible use of "war funds that are involved with seized assets" to reimburse USACE for its work in support of DFI-funded contracts. On February 26, 2008, DoD legal and Comptroller staff sent an email to USACE indicating the Department had no legal objection to using seized and vested funds to pay outstanding balances attributable to actual contracts awarded for the benefit of the Iraqi people, but that these funds should not be used to reimburse USACE for any overhead expenses.

On March 5, 2008, USACE processed payment vouchers totaling about \$9.2 million to cover the unpaid expenditures. On May 15, 2008, USACE received formal written direction. Specifically, the Acting Deputy Chief Financial Officer, Office of the Under Secretary of Defense (Comptroller), in a memorandum to the Director for Resource Management, USACE, advised that "This memorandum serves as my approval to use the residual advanced seized funds to reimburse USACE for contracts completed for the Government of Iraq. The funds should only be used to pay balances attributable to actual contract payments, not to reimburse USACE for overhead charges."

SIGIR's concerns are that the records supporting this transaction are unclear about (1) the type of funds used to reimburse USACE, that is, whether these funds were seized asset funds or DFI funds, and (2) what exactly USACE is being reimbursed for. During our review we have been unable to separately account for DFI funds and seized asset funds because the funds have been commingled. Also, initially USACE identified the expenses it reimbursed itself for as "unpaid

in-house expenses.” After we provided a draft report for comment USACE officials told us that the expenses were not for overhead costs, rather the funds were largely for employees directly supporting DFI activities. A few days later, USACE explained in an email and in its formal comments that \$8.9 million was for actual contract expenses and \$0.3 million was for direct USACE labor and associated overhead. Because these explanations were received after our draft report was sent for review, SIGIR has not had the opportunity to verify the information. However, we are presenting this new information at the request of USACE.

## **Other DoD Components May Have Retained DFI Funds**

Preliminary indications are that USACE is not the only U.S. entity that may be retaining DFI funds. For example, in May 2008, the Army Audit Agency issued a report<sup>11</sup> indicating that the Assistant Secretary of the Army Financial Management and Comptroller had retained about \$16.5 million in DFI funds that were never distributed to fund managers. The report recommended that the Army query potential users of these funds and return unneeded funds to the GOI. SIGIR plans to conduct a series of audits to determine whether other DoD components, as well as other U.S. agencies, are holding DFI funds.

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<sup>11</sup> *Accounting for Seized Assets and Development Fund for Iraq Balances*, U.S Army Audit Agency, Audit Report: A-2008-0109-FFM, 5/22/2008.

# **Conclusions, Recommendations and Lessons Learned**

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## **Conclusions**

The GOI terminated its authorization for U.S. administration of the DFI program effective December 31, 2007; nonetheless, USACE currently has DFI contracts open and has retained DFI funds. However, DoD lacks adequate policy and guidance on the disposition and use of these funds. Consequently, it is unclear how the funds should be used.

Issues that remain in question are USACE's use of \$9.2 million to pay reimbursable work order expenses it incurred in support of DFI activities and the authority to continue to hold \$3.0 million of DFI funds in its suspense account. Also, once DCAA completes its audit of the \$2.2 million of DFI funds currently being held by Washington Group International, DoD needs to provide guidance on how those funds can be used. Lastly, guidance is also lacking on what to do with interest that might have been earned by contractors when DCAA disallowed payments made to them by USACE for costs that had not been incurred.

## **Recommendations**

SIGIR recommends that the Under Secretary of Defense (Comptroller)/Chief Financial Officer provide guidance to USACE on the

- 1) use and ultimate disposition of DFI funds that it and one of its contractors are currently holding,
- 2) whether GOI funds should have been used to pay reimbursable work order expenses, and
- 3) how interest that might have been earned by several contractors on disallowed payments should be used.

## **Lessons Learned**

Sound accounting practices are important to any organization and take on even greater importance when cash and other country's money are involved as is the case with DFI. Weaknesses in accounting for DFI funds have been extensively documented; therefore, similar mistakes should not occur in other overseas contingency operations such as Afghanistan.

## **Management Comments and Audit Response**

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SIGIR received written comments from the Office of the Under Secretary of Defense (Comptroller) and USACE. The Deputy Chief Financial Officer concurred with our recommendations and stated that guidance would be provided to USACE in January 2010. In the course of addressing agency management comments, we revised one of our recommendations to address a USACE concern about how the funds were used. SIGIR made a draft recommendation that the Comptroller provide guidance on whether GOI funds can be used to pay in-house and overhead expenses. USACE stated in its official comments that the funds were used to pay for direct in-house labor and overhead expenses associated with its DFI contracting activities. Our final recommendation states that guidance should be provided on whether GOI funds should have been used to pay reimbursable work order expenses. This addresses the general nature of how DFI funds should be used. We informed DoD officials about the change from our draft report and they concurred with the final recommendation.

USACE also provided comments. Because our recommendations were directed to the Under Secretary of Defense (Comptroller) USACE did not comment on them directly. However, USACE disagreed with a SIGIR conclusion that \$9.2 million in GOI funds had been used to pay for in-house labor and overhead expenditures associated with its DFI activities. According to USACE, it determined after it received the draft report that \$0.3 million of the \$9.2 million was used to pay direct labor and associated overhead expenses in support of DFI contracts, and that the remaining \$8.9 million was used for actual contract payments. Because this information was received after our draft report was sent for review, SIGIR has not had the opportunity to verify the data and make all of the changes requested by USACE. However, we have included this explanation in the report at USACE's request.

## **Appendix A—Scope and Methodology**

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### **Scope and Methodology**

In March 2009, the Special Inspector General for Iraq Reconstruction (SIGIR) initiated Project 9011 as the first in a series of reports that the Special Inspector General for Iraq Reconstruction (SIGIR) plans to issue on its evaluations of the extent to which U.S. government agencies can properly account for Development Fund for Iraq (DFI) funds they received. SIGIR's objectives for this audit were to determine whether the U.S. Army Corps of Engineers (USACE) can properly account for DFI funds it received. This audit was performed under the authority of Public Law 108-106, as amended, which also incorporates the duties and responsibilities of inspectors general under the Inspector General Act of 1978. SIGIR conducted its work during from March 2009 through September 2009 in the United States.

To determine the amount of DFI funding that USACE may have held following the December 31, 2007, termination of U.S. government stewardship, we first attempted to determine the total amount of DFI funds USACE received. We requested access to financial transactional data—receipts and disbursements—from the DFI sub-account maintained by the Federal Reserve Bank of New York. SIGIR is still working to gain access to government-wide accounting records at the Federal Reserve Bank of New York. We requested this information to gain insight into the distribution of funds to the various federal agencies including the total amount of DFI made available to USACE. SIGIR also asked USACE financial representatives to provide a report of DFI funding authorizations it received and related obligations and disbursements for each DFI-funded project. On two different occasions, USACE developed reports on its DFI funding activities. Based on other sources of data available from the public domain, we concluded and USACE agreed that the data as presented to us was not all-inclusive.

To gain preliminary insight into the amount of DFI funding that USACE was holding following the December 31, 2007 termination of the U.S. government's stewardship, SIGIR relied on information from its *Hotline* concerning potential improper contract and financial management practices, along with related information developed by the Defense Contract Audit Agency (DCAA) which disallowed payments USACE made to contractors for costs that were not incurred. We believe DCAA's findings are reliable for the purposes of this audit. We also examined and analyzed key correspondence and guidance prepared by a variety of USACE and other governmental entities concerning the proper use of DFI funds. We refer to this documentation, where appropriate, within the body of this report. We analyzed additional collaborative information obtained from a series of data calls and interviews with officials assigned to the USACE-Transatlantic Programs Center in Winchester, Virginia, and the Finance Center in Millington, Tennessee. Lastly, we held discussions with officials from the U.S. Army Finance Command in Indianapolis, Indiana, and the U.S. Department of the Treasury in Washington, D.C.

To ascertain the amount of funding that USACE should consider returning to GOI, we examined the rationale and basis for previous returns of funds to the GOI and considered the Minister of Finance's memorandum requesting that all unused DFI funds be returned to GOI by the end of December 2007.

The audit was conducted in accordance with generally accepted government auditing standards. Those standards require that SIGIR plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. SIGIR believes that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## **Use of Computer-processed Data**

To identify the total DFI funding that USACE received, we relied on information contained in the Corps of Engineers Financial Management System (CEFMS). While this data analysis is still incomplete, SIGIR considers the initial computer-processed data provided by USACE to be sufficiently reliable to support the conclusions and recommendations provided in this report. For example, we compared summary listings of DFI funding generated by CEFMS to other data contained in independent audit reports prepared for the Government of Iraq and the International Advisory and Monitoring Board. We determined that, to date, CEFMS generated information did not provide a comprehensive picture of USACE's DFI funding activities. We presented the results of our review in the body of the report.

## **Internal Controls**

To achieve the audit objectives, SIGIR discussed general operating procedures related to USACE's DFI financial management process. We also reviewed internal controls and processes that USACE used in managing and administering the DFI contracting process. We determined that internal controls within USACE's accounting system were not sufficiently transparent to easily track the DFI funding it received. To complete our review, we examined documents in the contract file and held discussions with key officials to gain an understanding of the internal controls governing the use of DFI. We also considered comments and conclusions contained in independent audit reports and management letters concerning DFI internal controls. These reports were developed for use of the GOI and the International Advisory and Monitoring Board. We did not examine the contractor's internal management and financial controls and other organizations outside of USACE. We presented the results of our review of internal controls in the body of this report as appropriate.

## **Related Audit Reports**

We reviewed the following applicable audit reports issued by SIGIR, the Department of Defense (DoD), the U.S. Army Audit Agency, DCAA, and the U.S. Government Accountability Office.

### ***Special Inspector General for Iraq Reconstruction***

*Administration of Contracts Funded by the Development Fund for Iraq, SIGIR 05-008, 4/30/2005.*

*Iraq Reconstruction-Lessons in Contracting and Procurement, SIGIR, July 2006.*

*Management of the Iraqi Interim Government Fund, SIGIR 06-31, 10/27/2006.*

*Follow-up on SIGIR Recommendations Concerning the Development Fund for Iraq (DFI), SIGIR 06-36, 1/29/2007.*

*Iraq Reconstruction-Lessons in Program and Project Management, SIGIR, March 2007.*

*Attestation to Development Fund for Iraq Cash in the Possession of the Joint Area Support Group-Central, SIGIR 08-012, 4/13/2008.*

### ***Department of Defense***

*Internal Controls Over Payments Made in Iraq, Kuwait and Egypt, Department of Defense, Inspector General, Report No. D-2008-098, 5/22/2008.*

### ***U.S. Army Audit Agency***

*Accounting for Seized Assets and Development Fund for Iraq Balances, USAAA, Audit Report: A-2008-0109-FFM, 5/22/2008.*

### ***Defense Contract Audit Agency***

*Report on Voucher No. 151-FM-061, Dated November 9, 2006, Under Prime Contract No. DACA78-03-D-0006, D.O. 0002, DCAA-02161-2008V17900002, 1/31/2008.*

*Report on Voucher No. 58, Dated November 9, 2006, Contract No. DACA78-03-D-0005, Task Order 0006, DCAA-4411-2008N17900005, 8/20/2008.*

*Report on Voucher No. 1409-27, Dated November 9, 2006, Under Prime Contract No. DACA78-03-D-0004, Task Order 0002, DCAA-4261-2008W17900004, 9/5/2008.*

### ***U.S. Government Accountability Office***

*Recovering Iraq's Assets: Preliminary Observations on U.S. Efforts and Challenges, GAO-04-579T, 3/18/2004.*

*Stabilizing and Rebuilding Iraq: Iraqi Revenues, Expenditures, and Surplus, GAO-08-1031, 8/5/2008.*

*Stabilizing and Rebuilding Iraq: Iraqi Revenues, Expenditures, and Surplus, GAO-08-1044T, 9/16/2008.*

### ***International Advisory and Monitoring Board***

*Development Fund for Iraq, Statement of Cash Receipts and Payments, for the period from 29 June 2004 to 31 December 2004, Independent Auditor's Report, KPMG, 4/6/2005.*

*Development Fund for Iraq, Statement of Cash Receipts and Payments, for the period from 1 January 2005 to 30 June 2005, Independent Auditor's Report, KPMG, 9/29/2005.*

*Development Fund for Iraq, Statement of Cash Receipts and Payments, for the period from 1 July 2005 to 31 December 2005, Independent Auditor's Report, Ernst and Young, 9/13/2006.*

*Development Fund for Iraq, Statement of Cash Receipts and Payments, for the year ended 31 December 2006, Independent Auditor's Report, Ernst and Young, 7/5/2007.*

*Development Fund for Iraq, Statement of Cash Receipts and Payments, for the year ended 31 December 2007, Independent Auditor's Report, Ernst and Young, 6/12/2008.*

## **Appendix B—Acronyms**

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<b>ACRONYM</b>	<b>DESCRIPTION</b>
CEFMS	Corps of Engineers Financial Management System
CPA	Coalition Provisional Authority
DCAA	Defense Contract Audit Agency
DFI	Development Fund for Iraq
DoD	Department of Defense
GAO	U.S. Government Accountability Office
GOI	Government of Iraq
JCC-I/A	Joint Contracting Command-Iraq/Afghanistan
SIGIR	Special Inspector General for Iraq Reconstruction
TAC	Transatlantic Programs Center
USACE	U.S. Army Corps of Engineers

## **Appendix C—Audit Team Members**

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This report was prepared and the audit conducted under the direction of David R. Warren, Assistant Inspector General for Audit, Office of the Special Inspector General for Iraq Reconstruction.

The staff members who conducted the audit and contributed to the report include:

Benjamin H. Comfort

M. Glenn Knoepfle

Jason G. Venner

L. Michael Welsh

## **Appendix D—Management Comments**

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COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
1100 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1100

OCT 22 2009

**MEMORANDUM FOR ASSISTANT SPECIAL INSPECTOR GENERAL FOR IRAQ  
RECONSTRUCTION AUDITS**

**SUBJECT:** Comments to Draft Audit Report, “Development Fund for Iraq: Policy  
Guidance Needed to Enhance Accountability of USACE-managed Funds”  
(SIGIR 10-006)

This memorandum forwards the Under Secretary of Defense (Comptroller)  
response to the subject draft Special Inspector General for Iraq Reconstruction report,  
dated October 16, 2009. A copy of the response is attached.

We appreciate the opportunity to comment on the draft audit report. My staff  
point of contact is Ms. Audrey Clark. She can be reached by telephone at 703-602-0370  
or email at [audrey.clark@osd.mil](mailto:audrey.clark@osd.mil).

Mark E. Easton  
Deputy Chief Financial Officer

Attachment:  
As stated

SIGIR DRAFT REPORT - DATED OCTOBER 16, 2009  
SIGIR 10-006

"DEVELOPMENT FUND FOR IRAQ: POLICY GUIDANCE NEEDED TO  
ENHANCE ACCOUNTABILITY OF USACE-MANAGED FUNDS"

OFFICE OF THE UNDER SECRETARY OF DEFENSE (COMPTROLLER)  
(OUSD)(C) COMMENTS TO THE SIGIR RECOMMENDATIONS

**RECOMMENDATION:** SIGIR recommends that the Under Secretary of Defense (Comptroller)/Chief Financial Officer provide guidance to USACE on:

1. The use and ultimate disposition of Development Funds for Iraq (DFI) funds that it and one of its contractors are currently holding;
2. Whether the Government of Iraq (GOI) funds can be used to pay in-house and overhead expenses associated with DFI contracts; and
3. How interest that might have been earned by several contractors on disallowed payments should be used.

**OUSD(C) RESPONSE:** Concur. The Deputy Chief Financial Officer will issue guidance to USACE and other DoD Components to: (1) clarify the use and ultimate disposition of DFI funds; (2) determine whether GOI funds can be used to pay in-house and overhead expenses associated with DFI; and (3) determine how interest that might have been earned by contractors on disallowed payments should be used. Estimated completion date is January 2010.

Attachment  
Page 1 of 1



**DEPARTMENT OF THE ARMY**  
U.S. Army Corps of Engineers  
441 G Street, NW  
Washington DC 20314-1000

REPLY TO  
ATTENTION OF:

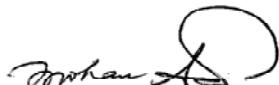
CEMP-GR

**MEMORANDUM FOR SPECIAL INSPECTOR GENERAL IRAQ RECONSTRUCTION**

**SUBJECT: USACE Response to 10-006 - Development Fund for Iraq Policy Guidance  
Needed to Enhance Accountability of USACE-Managed Funds**

1. The U.S. Army Corps of Engineers (USACE) appreciates the opportunity to review the draft report and the efforts made to address our concerns.
2. As the recommendations were directed to the Under Secretary of Defence (Comptroller), USACE provided comments concerning the recommendations to that office.
3. Subsequent to the release of the draft report, USACE established that only \$0.3M of the \$9.2M in delinquent DFI cost reimbursement was used to pay for At Cost direct labor and associated overhead in support of DFI contracts. The remaining \$8.9M was for actual contract payments. Supporting documentation was forwarded to SIGIR staff on 21 Oct 09.
4. Additional detailed comments are provided in the attached.
5. My points of contact for these comments are: Mr. John Daley (202) 761-5844 and Mr. Ken Littlefield (202) 761-5750.

Encl

  
Mohan Singh, P.E.  
Chief, Gulf Regional Team, SES  
Directorate of Military Programs

## **Appendix E—SIGIR Mission and Contact Information**

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<b>SIGIR's Mission</b>	Regarding the U.S. reconstruction plans, programs, and operations in Iraq, the Special Inspector General for Iraq Reconstruction provides independent and objective: <ul style="list-style-type: none"><li>• oversight and review through comprehensive audits, inspections, and investigations</li><li>• advice and recommendations on policies to promote economy, efficiency, and effectiveness</li><li>• deterrence of malfeasance through the prevention and detection of fraud, waste, and abuse</li><li>• information and analysis to the Secretary of State, the Secretary of Defense, the Congress, and the American people through Quarterly Reports</li></ul>
<b>Obtaining Copies of SIGIR Reports and Testimonies</b>	To obtain copies of SIGIR documents at no cost, go to SIGIR's Web site ( <a href="http://www.sigir.mil">www.sigir.mil</a> ).
<b>To Report Fraud, Waste, and Abuse in Iraq Relief and Reconstruction Programs</b>	Help prevent fraud, waste, and abuse by reporting suspicious or illegal activities to the SIGIR Hotline: <ul style="list-style-type: none"><li>• Web: <a href="http://www.sigir.mil/submit_fraud.html">www.sigir.mil/submit_fraud.html</a></li><li>• Phone: 703-602-4063</li><li>• Toll Free: 866-301-2003</li></ul>
<b>Congressional Affairs</b>	Hillel Weinberg Assistant Inspector General for Congressional Affairs Mail: Office of the Special Inspector General for Iraq Reconstruction 400 Army Navy Drive Arlington, VA 22202-4704 Phone: 703-604-0368 Email: <a href="mailto:hillel.weinberg@sigir.mil">hillel.weinberg@sigir.mil</a>
<b>Public Affairs</b>	Daniel Kopp Assistant Inspector General for Public Affairs Mail: Office of the Special Inspector General for Iraq Reconstruction 400 Army Navy Drive Arlington, VA 22202-4704 Phone: 703-428-1217 Fax: 703-428-0818 Email: <a href="mailto:PublicAffairs@sigir.mil">PublicAffairs@sigir.mil</a>

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